



TERRY E. BRANSTAD, GOVERNOR

IOWA UTILITIES BOARD
IOWA DEPARTMENT OF COMMERCE

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December 22, 1998

DEC 23 1998

FCC MAIL ROOM

Office of Secretary
Federal Communications Commission
445 Twelfth St., SW, Room TW-A325
Washington, DC 20554

RE: Federal-State Joint Board on Universal Service,
CC Docket No. 96-45, DA 98-2410

Dear Secretary:

Enclosed for filing in the above docket are an original and twelve copies of the Comments of the Iowa Utilities Board on the above noted docket.

Please stamp one of the enclosed copies, and return it in the enclosed postage-paid envelope.

Sincerely,

William H. Smith, Jr.
Federal & Legislative Programs Coordinator

Enclosures

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DEC 23 1998

FCC MAIL ROOM

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of

Federal-State Joint Board on
Universal Service

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CC Docket No. 96-45
DA 98-2410

COMMENTS
OF THE IOWA UTILITIES BOARD

The Iowa Utilities Board (IUB) submits the following comments in response to the Universal Service Joint Board's *Second Recommended Decision*, addressing the Common Carrier Bureau's November 25, 1998, Public Notice (DA 98-2410).

Summary

The Joint Board's *Second Recommended Decision* will not adequately provide for universal service as required by the Telecommunications Act of 1996 (96 Act). The IUB has particular concerns about how federal universal service funding is calculated and distributed among states.

- A smaller geographic area such as a wire center or exchange should be used in measuring costs as using a study area level would lead to insufficient support for truly high cost areas and would give support to areas that are not truly high cost.
- The FCC should set a precise benchmark that will assure "reasonably comparable" rates between rural and urban states.

- The FCC should not use revenue to measure a state's ability to support its own high cost areas because it is a misleading measure of a state's resources.
- The FCC should not maintain current funding inefficiencies through a "hold harmless" principle.

A smaller geographic area such as a wire center or exchange should be used in measuring costs as using a study area level would lead to insufficient support for truly high cost areas and would give support to areas that are not truly high cost.

The goal of universal service in the 96 Act is to assure that consumers in rural and high-cost areas have access to high quality basic and advanced telecommunications services that are comparable in both offerings and rates to those services offered in urban areas. This requires the specific targeting of support to rural and high-cost areas and does not allow the averaging of these areas with urban areas.

Continuing the practice of providing universal service support for all lines within a company's study area will result in misapplied universal service funds as the study area contains both low cost areas and high cost areas. For example, in the Iowa U S West case that established the prices of unbundled elements, using the HAI model, U S West loop costs ranged from \$88.23 in the lowest density zones to \$14.48 in the most densely populated zones.

Providing federal support to every line in the study area, instead of targeting the support to only the high cost areas, could encourage

uneconomic competition in the urban area and discourage competition in the rural areas. The competitor could serve only the urban area and receive federal support for lines that are low cost lines and should not require support. The support provided for the highest cost areas will not be sufficient and will discourage competitors from serving the rural areas. The incumbent local exchange company serving the entire study area with average rates will lose the customers in the urban areas that are providing support for the high cost rural loops.

Since the state sets the serving area for an eligible telecommunications carrier, the state could require a competitor to serve an entire study area. However, the FCC recognized in its May 8, 1997 Universal Service Order, this requirement could have the effect of prohibiting competition. The FCC stated, "we agree with the Joint Board that, if a state commission adopts as a service area for its state the existing study area of a large ILEC, this action would erect significant barriers to entry insofar as study areas usually comprise most of the geographic area of a state, geographically varied terrain, and both urban and rural areas. We concur in the Joint Board's findings that a state's adoption of unreasonably large service areas might even violate several provisions of the Act."¹

The Joint Board states, "As effective competition develops for high-volume, urban customers, one consequence may be erosion of the implicit

¹ May 8, 1997, Report and Order, CC Docket No. 96-45, ¶ 185.

support system that protects consumers in rural, insular and high cost areas from affordable rates.”² The Joint Board recognizes this erosion of implicit support will occur. The universal service fund should be the mechanism to replace the implicit support and target the support to the high cost areas. Instead the Joint Board is recommending a universal service fund calculation and distribution method that will not provide sufficient funding to the highest cost areas and will encourage the erosion of the implicit support.

The Joint Board at paragraph 25 says, “States possess the jurisdiction and responsibility to address these implicit support issues through appropriate rate design and other mechanisms within a state.” The IUB agrees the states can address the erosion of the implicit support through rate design and through a universal service fund. States can set up a universal service fund that targets the support to the high cost areas within the state. However, a state fund will not correct the problem created by the federal fund if the Joint Board’s recommendation is followed. The federal fund will still support urban areas that do not need support and will not provide sufficient funding to the high cost areas.

There is also the question of whether a state fund would be in violation of the 96 Telecommunications Act if it adopted a different methodology from the federal fund. The 96 Act provides, “A state may adopt regulations not inconsistent with the Commission’s rules to preserve

² November 25, 1998, Second Recommended Decision, CC Docket No. 96-45, ¶ 3.

and advance universal service.”³ This appears to be an area where the Joint Board is urging states to adopt “appropriate rate design and other mechanisms”⁴ to address implicit subsidies, while recommending the FCC abandon its pro-competitive policies and establish a federal fund that ignores the implicit subsidy issues.

Previously the FCC has urged geographic deaveraging in its recommended policies for universal service, unbundled network elements and eligible telecommunications carriers.⁵ Averaged rates cannot be maintained in a competitive environment; thus, it is important that the high cost fund target high cost areas and not base support on a statewide average. If the FCC accepts the Joint Board Recommendation of statewide averaging, it will abandon its previously established policies.

The IUB assumes the Joint Board is making this recommendation in order to maintain a small universal service fund. If the FCC sees a small fund as a desirable goal, the IUB urges the FCC to use some other means to control the size of the fund. Any mechanism set in place for the federal universal service fund should be consistent with competitive principles. Setting the calculation of support at the study area level is not consistent with competitive principles.

The IUB urges the FCC to look at other means of controlling the size of the fund, such as the U S West super benchmark approach. The IUB

³ 47 U.S.C. § 254(f).

⁴ Nov. 25, 1998, Docket No. 96-45 Universal Service Joint Board Second Recommended Decision, ¶ 25.

agrees that universal service is a shared responsibility. The federal mechanism should properly size the support needed for universal service and then determine the respective shares that should be born by the federal fund and the state fund. The IUB recommends an approach that would establish the entire support needed for each state and establish the maximum amount that a state should be required to bear to support universal service.

The FCC should set a precise benchmark that will assure “reasonably comparable” rates between rural and urban states.

The 96 Act requires “reasonably comparable” rates between rural and urban areas.⁶ However, the Joint Board has not given a meaningful definition of “reasonably comparable.” At paragraph 43 the Joint Board recommends a national average cost benchmark set at a level somewhere between 115 and 150 percent of the national average cost. The Joint Board states that its goal is to achieve reasonably comparable rates among states. If rates that are 15% above the nationwide average are reasonably comparable then it is difficult to understand how rates that are 50% above the nationwide average are also reasonably comparable.

If, for example, the average national cost is \$25.00, then the range that the Joint Board is recommending would be between \$28.75 and \$37.50. While one could reasonably argue that \$25.00 and \$28.75 are

⁵ May 8, 1997, Report and Order, CC Docket No. 96-45, ¶ 250.

reasonably comparable, it would be difficult to justify how \$25.00 and \$37.50 are reasonably comparable.

While the Joint Board recognizes that rate comparability among states can only be achieved through federal assistance, it also concludes that the total high cost support should be approximately what it is today.⁷ While the IUB agrees that the federal fund should be kept to a minimum, the IUB does not agree with arbitrarily setting the size of the fund. It appears as though the Joint Board has left the decision on the benchmark flexible so that the size of the fund can be controlled with the benchmark. This bottom-line type of approach will not achieve “reasonably comparable rates” or “sufficient funding” required by the Act.

The FCC should not use revenue to measure a state’s ability to support its own high cost areas because it is a misleading measure of a state’s resources.

The Joint Board proposed four alternative measures of a state’s ability to support its own high cost areas that could be used to determine the level of federal support to supplement a state’s ability to address its own needs.

The measures proposed⁸ were:

- The percentage of lines in a state with costs above a certain threshold;

⁶ U.S.C. 47 § 254(b)(3)

⁷ Second Recommendation, ¶ 48-49.

⁸ Second Recommendation, ¶ 44.

- Set each state's "presumed responsibility" at a given level expressed as a dollar value per line;
- The ratio of intrastate to interstate traffic volumes; and
- A percentage of intrastate revenue.

It is this last suggestion, the use of revenues as a measure, to which the IUB objects. The IUB agrees that states must take responsibility for some portion of their high cost access lines. The IUB does not, however, agree with methods that treat states differently for any reason other than actual differences in cost. The Joint Board's suggestion to use revenue as a basis for determining a state's ability to fund its own high cost areas results in different treatment among the states for reasons other than cost. Revenues are not a measure of a state's ability to support its own high cost areas. Revenues are, of course, directly related to the rates set by state commissions. When local service rates are set, considerations other than cost come into play. Different policy approaches employed in different states are integral to the determination of local rates. The fact that a company currently receives high cost support additionally determines rate-making. The Joint Board recognizes the distinction between rates and costs when it discusses the rationale for using costs, rather than rates, as a basis for a benchmark.⁹ The Joint Board's suggestion to use revenue here is inconsistent with that recognition.

The use of revenues as a measure would also lead to a result inconsistent with the FCC's long-held objectives of promoting efficient

⁹ Second Recommendation, ¶ 19.

competition by moving toward a rate structure based on cost. Using a revenue measure would penalize those states that have made progress on rebalancing rate structures and would reward those states that have not made progress.

The IUB suggests instead a progressive concept of federal responsibility for universal service, with increased federal shares where costs greatly exceed the national average. This concept is included in the “super benchmark’ approach mentioned earlier in these comments. For example federal support could be set at 100 percent of costs exceeding 150 percent of national average. The FCC should further consider alternatives that are based on actual differences in costs, rather than factors such as intrastate revenue that would confuse incentives for adopting efficient rate structures and introduce extraneous considerations into what is essentially a problem of differences in cost levels across the country.

The FCC should not maintain current funding inefficiencies through a “hold harmless” principle.

The FCC should move toward its goals of providing support in the most efficient manner and phase all non-rural companies into any new method of calculating support. The Joint Board’s recommendation that companies continue to receive explicit support at current levels would undermine the goal of efficiently targeted support.

In its previous recommendation the Joint Board recommended and the FCC adopted the use of proxy costs to determine support. The Joint Board said that these costs would represent the cost of an efficient competitor entering the market and would assure that the cost of services not included in the definition of universal service such as video, private line or interexchange services are not included in the support calculation.¹⁰ However, the current Joint Board recommendation would continue support to inefficient providers at the current support level based on current methods of calculating universal service.

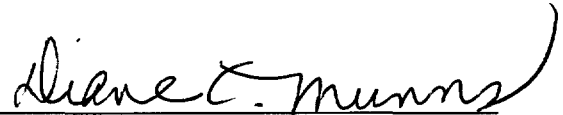
The IUB would not oppose a transition or phase-in of support from the current support to the support calculated using proxy models. However, companies should not be guaranteed current support indefinitely.

¹⁰ November 8, 1996, Recommended Decision, CC Docket No. 96-45, ¶ 270.

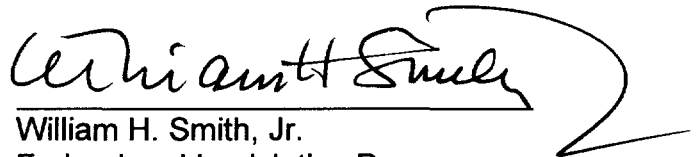
Conclusion

Therefore, the IUB requests that FCC reject use of the study area and adopt a wire center or exchange approach, set a precise benchmark to assure "reasonably comparable" rates, reject the use of revenue to measure a state's ability to support its own high cost areas, and not maintain current funding through a "hold harmless" mechanism.

Respectfully submitted,



Diane C. Munns
General Counsel
Iowa Utilities Board
350 Maple Street
Des Moines, Iowa 50319
(515) 281-4189



William H. Smith, Jr.
Federal and Legislative Programs
Coordinator
Iowa Utilities Board
350 Maple Street
Des Moines, Iowa 50319
(515) 281-6496

Johanna Benson
Senior Utility Analyst
(515) 281-5528

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